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RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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July 26, 1989 **LETTER 1022**

July 14 DJIA 2554.82; PTI 3143; A-D Ratio -6.76
July 21 DJIA 2607.36; PTI 3152; A-D Ratio -6.68
Dow Yield: 3.47; Dow P/E: 11.1; DowPow: 1019
Dow Book Value: 1075; Dow 200-day MA: 2299
Percentage of Undervalued blue-chips: 15%

THE MARKET: Last week saw the Dow rally above the 2600 level -- and close above that level for the first time since the crash. It amounted to almost a solo flight, however, for on the above-2600 Dow closing only 82 stocks on the NYSE recorded new 52-week highs. In all fairness, we've seen this phenomenon before, only to have the rest of the market catch up to the Averages. But I do get the feeling that the air is getting rather rarefied as the Averages (Industrials and Transports) probe new high ground.

The Transportation Average is now selling at almost double book value and with a minuscule dividend yield of 1.45%. The bulk of the upside action in the Transports is a reflection of airline takeovers or prospective airline takeovers (the current explosions being centered in UAL and AMR).

Because the Transport Average is made up of stocks that are highly leveraged, the Transport Average has always been used by Dow Theorists as a barometer of speculative sentiment. On that basis, I conclude (based on the current action of the Transports) that speculation in this market is intense. Much of this speculation, of course, is predicated on the ability of takeover artists to borrow and then write off the cost of debt.

Twenty-three months have passed since the 1987 bull market highs. During that time the D-J Transports have surged to new record highs, but the Industrials are still better than 200 points below their comparable bull market high. If the Industrials better their 2722.42 high, such action will be confirmation that the primary trend has remained bullish. Failure to better the '87 high will mean that we have seen one of the most remarkable (and deceptive) bear market rallies in stock market history.

PRIMARY TREND INDEX: I've said this before, but I want to repeat it for the benefit of new subscribers. These Letters can be read in two ways. (1) You can read it for my opinions, my interpretation of Dow Theory, and my personal ideas on the market, values and investing. (2) You can read it in order to track the action of my Primary Trend Index (PTI). No. 1 above is self-explanatory. So let's talk a bit about No. 2, the PTI.

The PTI is my proprietary indicator. The PTI is an amalgam of eight market averages and indices, each based strictly on market action (rather than sentiment or ratios of economic barometers). The PTI has nothing to do with the way I think, nothing to do with my own opinion, nothing to do with market psychology, or even with stock market values. The PTI is easy to follow: as I've said so often, "to follow the PTI, all you have to know is up from down."

For purposes of longer-term trend identification, I chart the PTI with an 89-day moving average (MA). Anytime the PTI is above its MA, the trend of stocks is up. Anytime the PTI is below its MA, the trend of stocks is down (see page 2 chart). Investors should align their stock positions with the PTI. Never be short when the PTI is in a rising trend. Never go long when the PTI is in a declining trend.

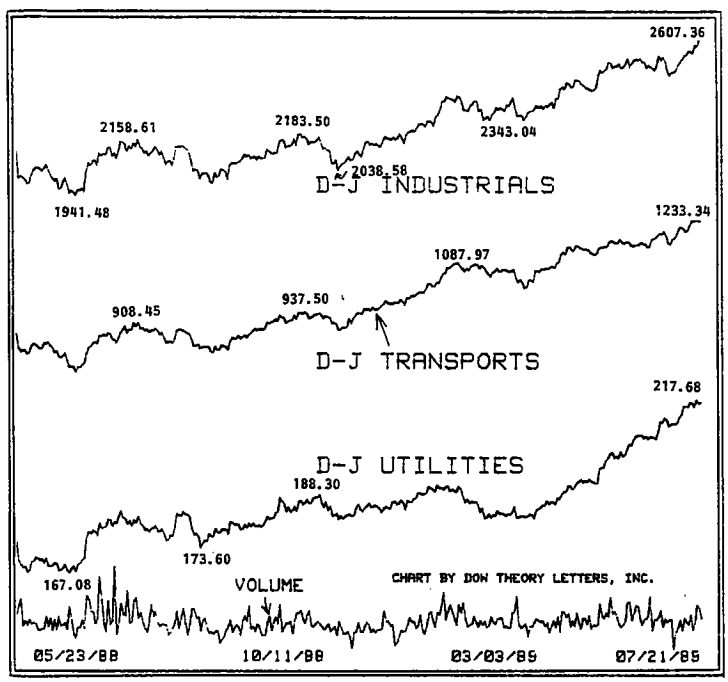
Following the crash, the PTI last turned bullish in January 1988. It has been in a persistent rising trend ever since. Only twice since January 1988 has the PTI even dipped to test (i.e. make contact with) its 89-day moving average.

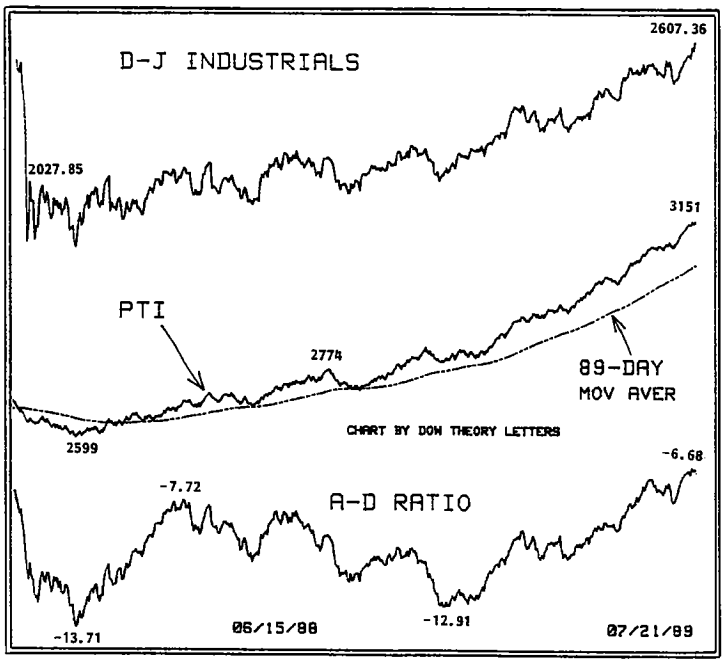
I started publishing charts on the PTI back in 1971, so this indicator has an uninterrupted 18-year history. By any reckoning, the PTI has been a winner. In the past the PTI has been a leading indicator, a coincident indicator and on occasion a lagging indicator. But investing (or divesting) on the basis of the PTI has put you on the right side of almost all the major moves of the market in the last 18 years.

One happy plus for the PTI is that it is not given to whipsaws. In other words, once the PTI defines a trend, it seems to stay on the right side of that trend for as long as that trend is in force. One common objection to the PTI is that following it represents "mindless investing." That's true in that the strict PTI investor is following an indicator that ignores absolutely everything but market action. But perhaps that's an advantage. If nothing else, one might call such investing the ultimate in technical analysis.

THE PICTURE: This is a rather unorthodox discussion. Instead of talking about what I think you should be doing, I'm going to tell you what I have been thinking and (right or wrong) what I've been doing.

As I said in the last few Letters, I am mostly out of the market. I still have a few bonds, and I still have some no-load stock funds (which I will trade on the basis of the PTI). But basically I now have the majority of my funds in muni cash funds. The fact is I made big profits on my bonds, and I wanted to capture some of those profits. It was strictly a personal decision. Profits for those of us who bought bonds back in the early to mid-1980s have been large to huge, and I guess long experience in the markets suggested to me to cash in some of those profits (see bond comments in "Investment Position" box).





The truth is that I'm thinking now in terms of what the next big "play" might be. I've said before that to make money, real money in the markets, you have to go into an item in a big way. Let's face it, you can't make big money in a bull market in stocks if you're in there with only 10% of your assets. And you can't make a killing in bonds if you have only $15,000 in the bond market. No, you have to be in there with a major position to make important money. There's no way of getting around that fact.

At this point I would not go into the stock market in a major way, and I would not go into the bond market in a major way. What about money market funds? A money market fund is for the person who is not sure. It's for the investor who has no strong opinions. The old Wall Street adage tells us, "When in doubt, stay out."

I find it beneficial every once in a while to move over to the sidelines and let the other fellow carry the ball. I know the market is always there. Furthermore, the unique thing about Wall Street is that you can leap in and invest a lifetime's earnings in five minutes -- and you can cash out just as quickly. But peace of mind is essential in this business (at least, it is to me). Right now I'm at ease, my mind is at rest, and I don't feel impelled to do anything "brilliant" today or next week or even next month. It's thinking time for Richard Russell, and here are some of my thoughts.

I've been an admirer of Stanley Salvigsen and Michael Aronstein, who used to write the quarterly Merrill Lynch report. They are now *Comstock Partners* at 45 Broadway, NYC 10006. In their latest *Comstock Investment Strategy Review* they reiterate their basic ideas, ideas which I must admit correspond with many of my own.

As you know, I have long held the view that this nation is killing itself with debt. In the next month or so Congress is going to face the distasteful job of having to raise the Federal debt limit to $3.2 trillion. That fact alone should tell you how serious the situation is. The interest on the US federal debt ($169 billion or $3.2 billion a week) is now the second largest item in the budget. And worst of all, the entire federal debt is COMPOUNDING at an alarming rate.

All my subscribers must know by now that I advocate compounding one's assets. This is the procedure that I term "the royal (and safe) road to riches." I also call this process positive compounding. When you have assets (and a modicum of debt) you can compound positively. But how about negative compounding or compounding in reverse? That's what happens when the cost of carrying your debt is greater than your income. And, of course, that's what our government is doing via its never-ending debts and deficits. Those debts and deficits are eating this nation alive.

Aside from the compounding process, we also see that the federal government has taken on hundreds of billions of dollar in contingent liabilities (i.e., guarantees). In short, the government seems to have guaranteed the solvency of anything and everything. And we're beginning to see some of the consequences of this "Uncle Guarantee-it-all" policy. We (the taxpayers) now have to ante up for the S&L bailouts, the bank bailouts, the VA and FHA and Ginnie Mae bailouts, and the coming HUD bailout, among others.

Comstock's contention is that interest rate costs are now compounding faster than the actual productive output of the US economy. In other words, as our massive debt structure compounds and expands, it is sopping up more funds than the economy can produce. Interest costs are beginning to devour the system.

To make matters worse, over the past decade US businessmen have gone on a leveraging binge, pushing up debts to even higher levels than the fat levels of the early 1980s. This has led to VULNERABILITY and in an increasing number of cases -- DISTRESS.

Comstock views this overall debt compounding process as basically deflationary. Ultimately, all debts must be paid off, refunded, defaulted on, or inflated away. The US government doesn't want to default (if it defaulted, how could it continue to borrow more?), and it can't pay off its debt. So the government follows two routes -- it refunds and it inflates. But the inflation process, so popular since World War II, is not that easy today. The money markets have become highly sensitive and sophisticated, and at the slightest hint of rising inflation, interest rates ratchet up, thereby confronting inflation head on. So the days of the simple "inflation remedy" are numbered. The sophisticated money markets and instant communications have seen to that.

Surveying this whole picture (and believing that it is basically deflationary), *Comstock* has opted for a major position in the longest-term Treasury debt. They have also assumed what they term a "defensive profile" in equities. In other words, they want to be in the safest long-term bonds (preparing for deflation) and very conservative as far as equity positions are concerned.

What do I think? I think it's a fairly intelligent position. But . . . but here is my own possible or potential objection to the *Comstock* view. First, in the event of a true recession (which, one of these days, we will most definitely experience) there is going to be a major shortfall in tax receipts to the US government. The specter of contracting business and an accompanying shortfall in tax receipts will produce huge new federal deficits, perhaps on the order of three or four hundred billion or more in a single year.

If that happens, the US Treasury will have to come into a panicky market for hundreds of billions of dollars in new money. In the face of massive Treasury borrowing, the dollar and bonds will collapse. As bonds collapse interest rates will go through the roof. This will produce an interest rate spike, a spike perhaps taking bond yields to, or even above, the 1982 highs. In this scenario the bad news will be that surging interest rates will knock business to its knees. The good news will be that investors with cash will be able to buy Treasury bonds at great bargain prices with accompanying juicy yields.

To get back to the present situation, it's obvious that today's debt-ridden economy would be very vulnerable in the event of a recession. This point has not been lost on the Fed. Over the last month the popular view that a "soft landing" is in the cards has given way to the view that a hard landing could be the possible fate of the US economy. In reponse to sliding durable goods orders, flat or falling retail sales and sliding auto and home sales, the Fed has moved quickly to ease Fed funds, inject funds into the banking system, and to encourage at least a few banks to drop their discount rate.

One question on my mind, in view of the Fed's easing action, is whether the dollar will weaken and whether inflation is fated to heat up again. The Fed's balancing act (balancing between inflation and recession) is becoming increasingly difficult, particularly since the results of any Fed action are often not felt for many months to even a year or so into the future.

If the Fed is unwilling to accept even a mild recession, then I would not be surprised to see inflation heat up again. And if that happens we should see hints of it in the action of gold. (Is that why gold has held at the 460 support level and seems to be building a base here?)

This view suggests the wisdom of at least a "diversification position" in gold (which I have been suggesting). Of course, the argument against gold is that US or world deflation would be a negative for gold. But in a real deflation, I believe the viability of our entire debt-ridden banking system could come into question, in which case there could be a rush for real money -- gold.

"Gold," you growl, "but gold has been going down or sideways for the past decade. Can't you find some items that is more exciting than gold?" All very true, but do you remember back in the early '80s when bonds were acting like lead sinkers? Do you remember when dear old Franz Pick used to advertise that "BONDS ARE GUARANTEED CERTIFICATES OF CONFISCATION?" And do you remember when all the advisors started repeating that catchy phrase about certificates of confiscation? But the real catch was that Pick was talking about history, about the bond market from 1946 to 1980, about <u>what was</u>, not about what was to be.

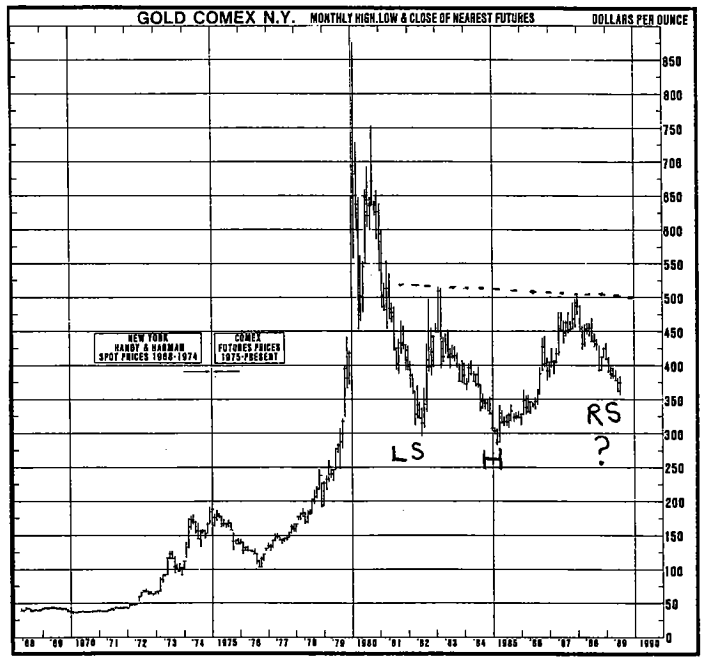
In the early 1980s bonds began to look like bargains, bargains that everyone hated -- but bargains nevertheless. I started buying the bonds around 1982, and I was almost embarrassed to do so. At the time, it was tough summoning up the courage to tell subscribers I thought bonds represented a bargain investment area, and high-grade bonds should be accumulated.

It took a few years (quite a few, in fact), before it was generally recognized that a 9% or 10% tax-free return on a high-grade municipal bond represented a bargain, but eventually values will out. (Today, advertisements in our local newspapers tell us that 6.5% muni bonds are a bargain, and, of course, today it "feels" easy to buy bonds.)

To get back to my original thought, I have asked myself a thousand times whether gold is worth accumulating here. Does it meet the criteria? Is it out of favor? Does everyone hate it? Is gold sold out? Is everyone convinced that it is going down? The answer in every case, I believe, is yes. In view of all this disfavor, IS gold actually going down now? And the answer is -- well it WAS going down, it hit a low of 359 a few months ago, but today gold is still holding well above its 359 low.

I've referred to the potential "head-and-shoulders bottom" in gold a number of times, but perhaps I should include this monthly chart again (chart courtesy of *Commodity Research Bureau*). Here we see Comex Gold in what could be a giant head-and-shoulders bottoming formation. If true, then gold is in the process of forming the right shoulder. A first bullish objective would be bettering 390, a second would be bettering 400, but the major objective would be completing the H&S bottom by rising above the major resistance at 500 (dotted line on chart). Will gold do it? The black pessimism, the adverse sentiment and the chart formation are all correct for a bear market bottom. But only time will tell.

So much for gold. What else am I thinking about? The economic expansion (boom) this nation has been experiencing is now going into its eighth year. Normally, at this point, the economic forces would "want" a rest or a correction. The consumer, after many years of non-stop buying, is retrenching a bit (we can see it in the sliding retail sales). At the same time takeovers and leveraged buyouts (now going global) have been fueling the market. But these takeovers and leveraged buyouts have also been loading the system with ever more debt, much of it dicey or questionable debt.



In the face of the economy's need for rest, the Fed appears fearful of a corrective recession. Without a correction, the economy will become increasingly vulnerable to inflationary trouble. Furthermore, the higher the stock market climbs without a rest or correction the more vulnerable it will be to a bear market.

So that's how I see the picture. At this point each stockholder and bondholder will have to decide for himself or herself how long to play the game. The danger signals are there, but most of them are rather subtle. In fact, I can almost guarantee that it will <u>not be as easy</u> to identify the top of this rise as it was to identify the top in 1987 (the market never gives us an easy or obvious repeat of an earlier event).

Personally, I have elected to "cool it," but that's just a personal choice. I have nice profits to show for my efforts since 1982. And at this point I'm willing to wait for the next act in the drama. I'm not greedy. If the Dow goes to 3,500 I'll just have to be a fascinated observer (although I still have a small position in no-load funds). If long-term T-bond yields drop to 6% I'll just have to be an interested spectator (although I have kept some bonds but not too many).

In deference to the bulls, the PTI continues to make new highs. As a matter of fact, this has to go down as one of the most persistent and spectacular advances in the PTI of the past 18 years. Furthermore, the PTI has not yet lost its upside momentum.

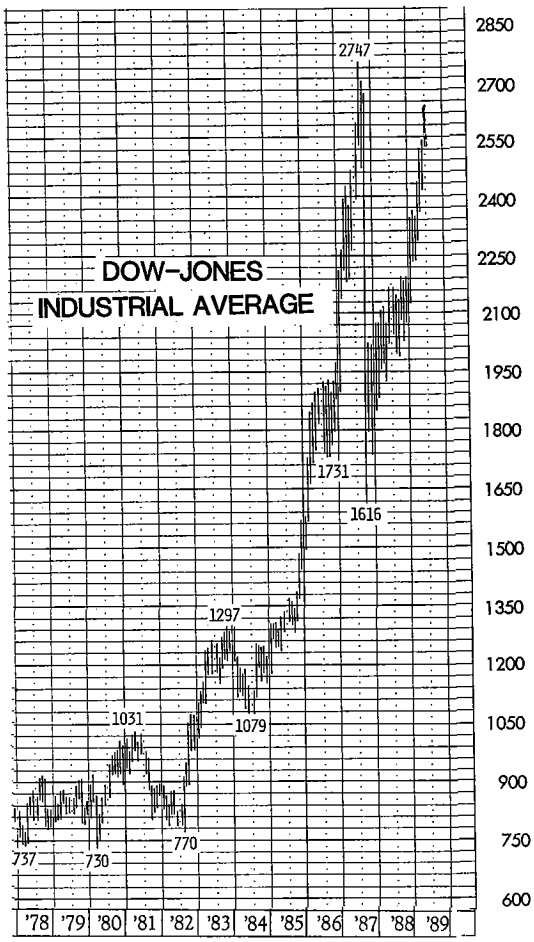
But in this business "each man has to kill his own snakes." At times (as veteran subscribers know), I've been extremely positive about the outlook for the market. At other times (as now), I lapse into uncertainty. But that's all right with me. I'm an old hand at living with uncertainty.

At this point the majority of my money is compounding in muni cash funds. And that sits well with me. I simply treat it as an exercise in anti-greed. And, of course, it also fits in well with Russell's First Investment Principle, which states, "Above all, lose no money."

<u>Comments:</u> At various times (and they are rare) a market movement seems to take on <u>a life of its own.</u> This appears to be one of those times. I can see it in the relentless action of my PTI. How do such movements end? They end in only one way -- <u>exhaustion</u>. As this is written one thing is obvious: this market is <u>not exhausted on the upside</u> -- not yet.

I don't want to be a "market sissy," but I note that the monthly arithmetic chart of the Dow is looking rather wild. On this chart by

Horsey we see the Dow roaring up in a two-spike formation -- one from 1984 to 1987, followed by the crash. Then we see a new spike starting from the 1987 low and currently pushing to within striking distance of the 1987 high (Dow 2722.42). How the whole thing progresses from here and how it ends is anyone's guess. But one thing is sure -- the 1988-89 stock market is carving out a dramatic niche for itself in the drama and history of Wall Street.



Earnings note: *Industry Forecasts* written by the Levys out of Chappaqua, NY, in their latest report note "the 'real' after-tax earnings of non-financial corporations, after rising 6% from the third to the fourth quarters of 1988, fell in the first period of this year. . . . A steeper fall will occur in the quarter just begun. Corporate earnings in the second half will be far below those of the corresponding 1988 period." Russell comment: Is this why the Dow has refused to rally to new highs?

INVESTMENT POSITION: Last week I received a letter from the Vice-President/Investments for a large brokerage firm in LA. The letter runs as follows: "I just had a conversation with my brother who is a CPA. He says inflation in California is actually 9%, and keeping money in municipal money market funds is a bad investment. He tells me that real estate is the only way to fly. Problem: real estate isn't a great value. Any advice?"

I don't have any advice, but I do have a few thoughts. (1) The markets are always there. (2) Patience is a virtue. (3) Muni money market funds are no bargain, but tax-free money at 5.5% isn't exactly a hardship either. (4) At times there is nothing brilliant that one can do. But there is something intelligent that one can do. The most intelligent thing you can do when you don't perceive any great value areas is -- don't lose money.

(5) The time-honored axiom for success on Wall Street is to "go with the flow." If you can't detect any definite flow -- sit tight in a safe place, and wait until you do perceive a bullish flow. Ignoring Axiom 5 ultimately wipes out 95% of the commodity traders and a majority of stock traders.

For those who have stocks, bonds, or cash I say again, "sit tight." I don't see anything brilliant to do at the moment or any brilliant switch to make. As a matter of interest, the percentage of undervalued blue-chips on the NYSE (see statistics on page 1) has now dropped to 15%, the lowest figure of the entire post-crash recovery. In the past, that's not been a good omen.

Comment: The current unanimity on the subject of the direction of interest rates is truly remarkable. I read report after report ALL stating that interest rates are heading down. Can everybody be right? They can at times, but it does make me suspicious. What could make everyone wrong on the rates? Answer: No recession at all (and with even the slowdown behind us), or perhaps stagflation with an accent on the inflation. That scenario would seem to fit in with the current action of the stock market.

MOM: My mother was born in 1898. Last March II she turned 91. My mother is bedridden now. She lies there with her still-blonde hair and her sunken blue eyes, and sadly, she has pretty well lost interest in life. "I'm too old," she says wistfully, "I've lived too long." I tell her that there are people in her building (it's a rest home) who are over 100, but mom knows herself better than anyone. She is convinced that she's "lived too long," and she's already prepared to leave this Earth.

Sensing all of this coming, I made an audio tape of my mother about 10 years ago. I asked her to tell all she could remember of her life. Then about three years ago I made a videotape of mom, and I again questioned her about her life. She talked on each tape for about an hour. I questioned her, and she spun out the many colorful stories of her life.

I'm glad I made those tapes. I couldn't make them now. I want the tapes for my kids and my grandchildren and their kids and their grandchildren. I think it's a shame that we don't know more about our forefathers and foremothers. Each one of us has gone through struggles, adventures, wars, marriages, happy times and tragedies, and each one of us has amazing stories that we could tell. But think of the generation after generation whose life stories are lost forever, lost in the dust and darkness of history.

What I wouldn't give to have tapes of my own father, my father's father and the men and women who led up to my own birth. Every one of us is curious about the circumstances of our existence. But probably 98% of the real stories of our pre-history is lost -- gone and irretrievable.

I think of my mother. She was born before the turn of the century. She saw the world before there were cars, radios, movies, TV. She lived through two World Wars, the Great Depression and the boom years. In her lifetime she saw the rise of American power, she saw America change from the world's greatest creditor to the world's greatest debtor. My mother is living history, and I have at least some of her stories on tape.

I remember many stories my father told me (he died in 1956). He was born in Washington DC, but when his father died (by suicide) he and his mother moved to Orangeburg, South Carolina. Then my father moved north, borrowed enough money to go to and graduate as an engineer from Columbia University. During WW I he met my mother, and, well I could go on and on.

I have only pictures of my father and memories plus many photo albums he carefully put together. But what I wouldn't give for a few hours of videotapes of my dad, as he told of the experiences and adventures of his life. So as I write this I want to send the message to my subscribers. Get your folks on tape. Get yourself on tape. If you have kids or relations, they'll treasure those tapes one day.

NOTES & QUOTES: What's the most popular cable network? It's ESPN, the sports network, which now goes to 56% of all the cable hook-up homes in the US.

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Speaking of sports, the new *National*, an all-sports newspaper, is scheduled to appear in the fall or thereabouts. It will be a daily paper in color costing 50 cents. The new paper will put pressure on *USA Today* (whose sports section is tops and is a big attraction), on the weekly *Sporting News* and most definitely on the bi-monthly *Sports Illustrated.*

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Finally, having succeeded with ESPN and MTV, a new concept emerges -- 24-hour comedy. Both HBO and MTV plan around-the-clock comedy channels. This is interesting since a growing opinion has it that laughter (no kidding) constitutes an excellent treatment for diseases of all kinds. If so, cable comedy should make for a healthier America. One straw in the wind: Comedy clubs have proliferated, and there are now nearly 400 in the US.

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The Japanese money supply has been booming for many years, so there are plenty of yen around in Japan. Nevertheless, Japanese savings have been little short of phenomenal. In 1988 Japanese personal savings rose to $5 trillion, up 11% from the previous year and amounting to an incredible $12,600 per family. One reason for Japan's savings rate may be they have no Social Security. Therefore, Japanese believe they must save for their old age. Japanese families also put tremendous emphasis on education, and most families save to send their children to school and hopefully to the universities.

More on Japan: Japan is now the world's largest giver, earmarking $43 billion this year for foreign aid . . . Japan, with an economy 60% the size of the US's economy, narrowly passed the US in capital investment last year at $498 billion (vs. the US's $488 billion). Current estimates are that this year capital spending in Japan is exploding. The London *Economist* states "the Japanese economy is currently growing at a breathtaking 9.1% a year, moved along almost single-handedly by plant and equipment spending, which is galloping upwards at an annualized rate of 29.1%."

* *

I stated in the last Letter that I thought the key to the nation's economy was real estate (with $2.5 trillion in residential mortgages in the U.S.). The wealth of America's citizens lies in the value of their homes. Along these lines, it is worth noting the July II *WSJ* included an article entitled, "Real Estate Hits Slump in New England." The article goes on to state that the banks are being hurt as prices sag. "From Connecticut to Maine the biggest problem is the glut of condominium projects." But the following is important: "The reasons for the slowdown are clear enough. The median single-family home price in the Boston area, for example, rocketed to $167,800 in early 1986 -- highest level in the country at that time -- from $89,400 in 1984. Meanwhile, household incomes weren't rising nearly as fast, despite the region's healthy economy. By mid-1988, the median family income was $38,652, and the median home price was $183,800." In other words, the typical New England family couldn't carry the typical home. And the economy has weakened considerably over recent months.

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The last bastion of booming home prices is California. But here too housing is being priced out of the reach of the typical family. The end result, I feel, has to be a slump in home sales and then a slump in home prices. So far, we've only seen a slump in volume of sales of homes. If and when home prices across the nation start sliding, that's when we'll see the real trouble (of course, that's what has already happened in Texas and major areas of the Southwest).

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The current whoppping 5.5% yield spread between junk bonds and treasuries is causing Wall Street to wonder. Is the spread telling us that the junks are an overlooked bargain? Or is the spread telling us that the economy is heading down and the junks are in trouble? No help to junk bond sentiment is the widely-quoted, unnerving Harvard study which shows that 34% of all junk bonds sold during 1977-78 were in default by 1988.

Holders of junk bond ("high yield") funds got a further jolt in mid-July when they heard that Drexel Burnham had unloaded its eleven junk bond funds. Average losses to investors (who had purchased the funds during the 1980s) amounted to about 18%. So far this year, junk bond defaults have amounted to $3.2 billion.

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It's the same old disgusting story. Despite the recent postal hikes, the US Postal Service is again running deficits -- $125 million for May and probably $1 billion for the entire year. The problem: the PO refuses to cut costs. A recent study shows that if the PO would contract out certain areas to non-union carriers it could cut its $10 billion a year delivery costs in half. But the postal unions have a lot of clout with Congress, so it looks like instead of cost cuts at the PO we'll be paying 30 cents for first-class delivery in January 1991. Maybe it's poetic justice that the day of the fax is fast arriving.

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The France of old (the little bearded farmer carrying a loaf of bread) no longer exists. Since WW II France has converted from agrarian to urban (today only 7% of the French live in the country). France's economy is in second place in Europe and is 80% as large as West Germany's. France is an independent nuclear power with the world's third largest navy. France is also a world leader in fusion, medical research, computer software and weapons develpment. But the biggest change in France is its new-found interest in money and making money. It's all summed up by a French sociologist: all of a sudden "money doesn't smell bad any more."

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The Japanese spent $8 billion over the last 10 years building the 6-mile Seto Inland Sea Bridge connecting Honshu Island with Shikoku Island -- the final link in connecting Japan's four main islands. But few use the bridge. Problem: The round-trip toll for the bridge is $85.

* *

How is Wall Street faring? Often, the price of a seat on the NYSE tells the story, as far as the brokers are concerned. In 1987 a seat price climbed to a record $1.15 million. The fellow who bought that seat has reason to regret it. In May a seat sold for $500,000, and a few weeks ago on July 5 a seat sold for $550,000.

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Not escaping Wall Street's semi-depression is the newsletter business. Dan Dorfman (in *USA Today,* July 21) devotes a whole column on the disastrous slump in the industry. Here are a few excerpts:

> **The message is clear: Despite a peppy 1989 stock market, most investment newsletters continue to do lousy.**
>
> **That conclusion is based on discussions with a number of newsletter writers and talks they've had with colleagues. Overall, new subscriptions are said to be off 55% to 80% vs. '88. Renewals: Off 30% to 40%.**
>
> **What's more, barring a major change in investor psychology — unlikely in the face of continuing fears of a recession — there's little evidence that the newsletter business will turn around in the near future.**
>
> **What's wrong? Fosback, president of the Institute for Econometric Research in Fort Lauderdale, Fla., blames:**
>
> **▶ The 1987 stock crash, which caused many individual investors to flee the market. Even though stocks have rebounded, many individuals still haven't come back.**
>
> **▶ The continued presence of computer "program" trading, which still throws the market for a loop many days. That's still a scare for small investors.**
>
> **▶ The downfall of adviser Joseph Granville. A superstar in the late 1970s, he turned into a disaster in most of the 1980s. His collapse made many investors less trustful of newsletters.**
>
> **▶ Inside-trading scandals, which convey the idea to investors that "they can't beat the market because it's fixed and crooked," says Fosback.**
>
> **▶ The growing proliferation of "free" market advice from other sources — including TV, newspapers and magazines.**

Russell comment: Either I'm doing something right or I have the most devoted subscribers in the business. Subscriptions here continue to hover near 30-year highs, and subscription renewals to Dow Theory Letters have averaged 81% for the first six months of

this year. That represents probably the highest renewal rate in the industry. So at this point I do want to give a low bow to all my loyal subscribers and say "Thank you."

* *

Is the debt-laden American consumer nearing the exhaustion point? Retail sales have declined or not grown for six successive months (through May). This hasn't happened in the last 22 years!

* *

Popular Science magazine (August) sees the "loading of the atmosphere with carbon dioxide and other gases" resulting in "an accelerated greenhouse effect" as the major danger facing the world today. Think they're crazy? Note the following: 1988 was the hottest year of which we have any record -- and the five hottest years of this century all occurred during the 1980s.

* *

Last week Sidney Hook, the great author, philosopher, teacher and anti-totalitarian died. I was fortunate enough to have taken Hook's famous course ("The Philosophy of Democracy") at New York University back in 1945. Without a doubt Hook made a greater impression on me than any teacher I've had before or since. Hook was an original thinker and taught via the Socratic method of asking qustions. Hook took absolutely nothing for granted. Here's a typical story about Hook (who was a confirmed agnostic): a student asked him what he would do if he went to heaven and found that indeed there was a divinity. Hook retorted, I'd walk up to the Lord and complain, "But God, you didn't give me enough evidence."

* *

According to Professor David Gordon (New School for Social Research in NYC), over the past 15 years the real hourly earnings of 80% of US workers declined by more than 8% -- at an average annual rate of half a percent a year. Afer deducting taxes the total decline since 1973 was closer to 9% -- from $6.58 (in 1988 prices) to $6.01. This is the first time since the Civil War that workers have experienced an extended decline in real hourly wages. Even during the Great Depression of the 1930s real hourly wages rose -- by a mere 0.54% (due to severe deflation).

* *

Wall Street may be hurting but Hollywood isn't. For the first six months of 1989 theaters sold a record $966 million worth of tickets. Of course, Hollywood loaded up in early summer with many of its most promising moneymakers including "Batman" and "Lethal Weapon II."

* *

Sales of Hyundai, the bargain-priced S. Korean wonder car of a few years ago, have gone in the tank, dropping 45% this year over last. Dealers who had to pay $1 million to build free-standing showrooms to get a franchise are now screaming to be allowed to carry other makes.

* *

Vancouver ("Hong-couver") is taking on a decided Chinese look. Vancouver has the second largest Chinatown in North America; only San Francisco's is bigger. Vancouver is also overflowing with Hong Kong cash. The Hong Kong exodus figures: in 1986 19,000 residents left Hong Kong. In 1987 it was 30,000. In 1988 45,000. Half of all Hong-Kong emigrants moved to Canada.

* *

I just taped the remarkable one-hour PBS program on the life of jazz great, Charlie "Bird" Parker. Parker with his fabulous alto sax playing, along with trumpeter Dizzy Gillespie, revolutionized modern jazz. Bird was a heroin addict and an alcoholic. When he died in poverty in NYC the coroner on examination estimated the Bird's age at "55 to 65." Charlie Parker was 34 when he died.

* *

Speaking of drugs, if you've ever had an urge to "get a boost" with a snort of cocaine, see the movie, "The Boost." It's an outstanding movie with another fine performance by James Woods. When the film was over I could only shake my head and say, "Whew, this has to be the ultimate anti-drug movie."

GOLD: I wrote about gold in the first section of this Letter, so not much is needed here. Gold has moved above its short-term moving average, and it has also given an initial point & figure buy signal by rallying above 376. The next bull hurdle would be a move above gold's 200-day moving average, which is now about 396. The 396 level has proved to be a tough barrier on the upside for gold, so I would say that any rally above 396 (with an ability to hold above that figure) would be a most important one for gold. A move above 400 would reverse the entire declining trend, a trend that started from the 1980 all-time peak. The floor or support for spot gold seems to have moved up to around 365-68.

It may also be signficant that many of the S. African gold shares have given initial bull signals.

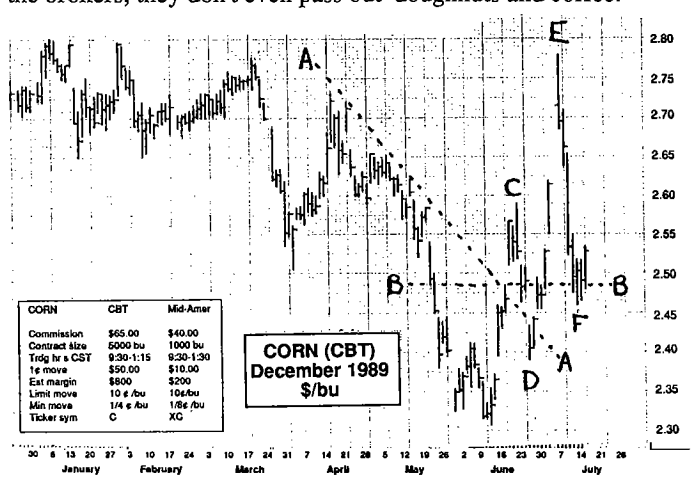
BEAT 'EM: Commodity traders, by the thousands, keep trying to beat the market. But about 95% of them lose money (although to tell the truth it is a barrel of excitement). Lest my beloved subcribers try to beat the commodity markets, let me show you what you might have to tangle with.

Admittedly, this year has been a particulary tough one for commodity traders, but let's examine the recent and current action of widely-traded corn (daily chart courtesy of my friends at *Dunn & Hargitt*). Corn went into a bear trend in April, hitting a low of 2.31 in June. The breakdown is defined by declining trendline A-A on the chart.

In early June it looks like a little base is forming, and when corn breaks above resistence line B-B you jump in to go long on a few contracts. At point C corn is almost up to 2.60, and you're feeling feisty. But corn suddenly plunges, hitting a low around 2.40 at D. You're a careful trader and you use stops, so you're stopped out at 2.45 for a nice loss.

Believing the rally has failed, you turn around and short corn at 2.44 a little above point D. Suddenly corn explodes to a high of 2.78 at E. Ouch, you've been killed on the short side. You take your losses again, and go long, because at E corn has even bettered its April peak, and a real trader knows when to reverse his stand and go with the trend. The advance looks like the real thing, and maybe on this run you'll make up for some of your losses. But after the spike at E, corn abruptly plunges, dropping intra-day (at F) below the resistence at B. You've been stopped out again, this time you've taken some killing losses.

So it's on the phone to your broker. "You've got margin calls," he tells you sorrowfully, "I've got to have money fast. Can you get over here with a check before the close" . . . And so it goes. You decide that this is tougher than Vegas. And in Vegas, you console yourself, at least they have those great, cheap buffet meals. As for the brokers, they don't even pass out doughnuts and coffee.



LATE NOTES: The spread between the PTI and its 89-day moving average at this writing is 110 points, the largest spread I've ever seen. Does this mean that the PTI is in a "power surge"? Or is the spread telling us that the market is exhausting itself on the upside? I can't tell, because I haven't seen anything like it before. But it does seem to me that the Dow has been spurting with fewer and fewer stocks following.

As for bonds, their action now hinges on the dollar's action. The bonds will not stand up against a weakening dollar. And the dollar won't stand up against weakening US interest rates. I believe the Chinese crisis brought a flood of money into the US, money looking for a safe harbor. That flood has now subsided.